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DISCUSSION GUIDE

Outlook 1990

National Economy and Agricultural Policy

Luther Tweeten

National Economy

The national economy has shown considerable resilience. Real gross national product grew at an annual rate of 2.5 percent in the second and third quarters of 1989. In late 1989, the economy was troubled by reduced housing and auto sales and by lower earnings in manufacturing.

Slide: Forecasts of Real GNP Growth, 1990

Estimates range from 1.7 to 2.6 percent. Not spectacular but fast enough to avoid recession and slow enough to avoid inflation. Most forecasts look to slightly slower growth in 1990 than in 1989.

Other predictions for 1990:

Inflation: 4.6%

Unemployment: 5.2%.

Things to watch:

Slower foreign income growth and a high dollar, potentially lower U.S. exports

Possible recession - 30 percent chance.

High real interest rates will continue but market rates of interest may fall if Federal Reserve continues to expand money supply to stimulate the economy.

Slide: Farm Debt Change and Real Interest Rate

Continued high real interest rates (market rate less inflation) in 1980s gave incentives for farmers to pay off debts. High real interest rates are one of the costs of mismanaged macroeconomic policies of the past.

Mostly, the national economy will be supportive of agriculture in 1990.

Agricultural Policy -- 1990 Farm Legislation

Background

1. Most say 1985 farm bill has worked and only needs modification.
2. Congress will take initiative for new farm bill.
3. Environmentalists will be active to promote food safety and protect water.
4. Farming economy different in 1990 than earlier.

<u>*Slide: Proportion of Farms Financially Vulnerable*</u>

The proportion of vulnerable farms (negative cash flow from all sources and debt-asset ratios of over 0.4) has fallen from 18% in 1984 to 11 percent in 1988 on commercial farms and from 12 percent in 1984 to 7 percent in 1988 on all farms.

<u>*Slide: Income and Net Worth, 1988*</u>

Net income from all sources on modest size commercial family farms with sales of $100,000-$250,000 was double the median income of all U.S. families in 1988. Net worth of the same size farms was at least 10 times that of nonfarm families with heads of similar age.

5. Some government objectives of the 1985 farm bill are being met. One of those objectives was to make U.S. agriculture more competitive in international markets through lower support prices.

<u>*Slide: Real Corn Support Rates, 1970-1988*</u>

Since the 1985 bill, <u>real</u> target prices have fallen nearly 30 percent and real loan rates even more. Administration will be reluctant to raise loan rates (to save on deficiency payment costs) because that would reduce international competitiveness. Reducing target prices further to save Treasury dollars is not politically popular.

<u>*Slide: Government Costs of Commodity Programs (CCC Net Outlays)*</u>

Government costs of programs have fallen from a peak of $26 billion in 1986 to an estimated $12 billion in 1990. Still, Congress and the Administration will be looking for new *savings.*

6. Stocks are down substantially.

<u>*Slide: Marketing Year Ending Stocks*</u>

Projected wheat, feed grain, soybean, and cotton stocks for 1990 are well below 1986 levels and are near levels economists consider to be optimal (desired). An exception is wheat which is well below minimal adequate levels. The government doesn't want to get back into costly support of huge stock levels.

Key Issues for 1990 Farm Bill

1. Cost of programs to government.
2. Flexibility in what to produce.
3. Environment.

These three key issues could be addressed by the <u>triple</u> <u>base</u> <u>plan</u>.

Example:

100 acre crop acreage base for corn
- 10 acre (10%) set aside to soil conserving uses
- 20 acre (20%) flex-use to be planted to whatever farmer chooses, such as corn, soybeans, hay, pasture, etc.

= 70 acres corn planted for harvest.

This would give flexibility (oats, soybeans, corn or other crops could be planted on corn flex-use base), reduce program costs (the deficiency payment would not be paid on the 20 flexible acres), and would help the environment by allowing a rotation (plant clover on the flexible-use acres). A problem is the cut in deficiency payment but that would be partly compensated by updating program yields and by greater cropping flexibility.

Another option is to go back to the normal cropland acreage (NCA) program of 1970. A farmer would set aside (say) 10 percent of NCA and plant whatever he desires on other acres. A problem with either proposal is how to handle deficiency payments.

Slide: Ratio of Target Price to Economic Cost of Production, 1986/87

Corn is most favored by target price relative to cost of production. To encourage flexibility, target price cannot be paid on all corn, wheat, etc. acreage. One option is to freeze acres and yields on which target prices are paid. But this decoupling raises questions of equity among farms and unequal inducements to participate in programs. If deficiency payment continues no matter what is produced, the public will increasingly question what payments are for.